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Washington, DC

REDUCING STUDENT LOAN DEFAULTS

A PLAN FOR ACTION

U.S. Department of Education
Washington, DC
Office of Planning, Budget and Evaluation

Introduction

The third largest expenditure by the U.S. Department of Education does not provide new financial aid to students nor improve science labs at colleges and universities. It goes out of the window, lost to student defaults.

Representative Tom Coleman (R-Mo)
NCEI Reports, February 18, 1988

There is no question that the taxpayer is paying—and paying dearly—for defaults under the [guaranteed student loan] program.

Senator Sam Nunn (D-Ga)
Hearings on abuses in federal student aid programs, February 20, 1990

Defaults are an epidemic threatening to become a habit.

Washington Post, September 2, 1987

We need action now to ensure that scarce student aid dollars are available to as many deserving students as possible.

Representative Marge Roukema (R-NJ)
Newark Star Ledger, June 26, 1989

UNITED STATES
DEPARTMENT OF EDUCATION

Our nation's future economic success depends on an educated and skilled work force. Technological advances increase the demand for a labor force that can adapt to a more complex workplace. According to the U.S. Department of Labor, more than half of all new jobs created over the next 20 years will require some education beyond high school, and almost a third will be filled by college graduates.[1]

The federal Guaranteed Student Loan (GSL) programs help students meet the challenges that lie ahead. They provide low-interest, long-term loans to students with demonstrated financial need to help them pay for their postsecondary education. In fiscal year (FY) 1990, 4 million students will participate in the GSL programs, borrowing approximately $11 billion.

As more people have received loans, the number of loan defaults and the associated federal costs also have increased. Default costs have risen eightfold since FY 1981. In fact, student loan defaults will consume nearly 44 percent of the entire $4.6 billion budget for the program in FY 1990. These statistics—and the publicity surrounding them—are bad for the loan program: they erode the program's integrity and endanger its future. Obviously, resources that are lost to defaults cannot be used to support the education of current and future students.

Last year, I announced an initiative to combat defaults. This handbook is part of our continuing efforts to protect students, increase accountability, and reduce default costs.

Students are not blameless for the defaults. However, defaults are one indicator that students are often being short-changed in their education. Behind the default statistics are students who are either unable or unwilling to repay their loans. Many of the defaults could have been prevented if everyone involved in student loans—students, postsecondary institutions, lenders, guarantee agencies, and the federal and state governments—had worked together.

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1 U.S. Department of Labor, *Opportunity 2000*, Washington, DC: U.S. Govt. Print. Off., September 1988, p. 14.

Only through such cooperation can we now restore integrity to the student loan program, help our students fulfill their loan responsibilities, and avoid leaving them in debt with little or no education. It is time for all participants to review the causes of default and develop a plan to deal with the problem.

This handbook is intended to offer postsecondary institutions, lenders, guarantee agencies, accrediting agencies, and states practical suggestions to reduce defaults. It is not intended for students. Students who have questions about the student loan programs or other aid programs can obtain a copy of the *Federal Student Aid Fact Sheet* from the Federal Student Aid Information Center (1-800-333-INFO).

We have profiled organizations that have employed interesting and innovative approaches to reducing defaults in the hope that their strategies might stimulate others to develop effective techniques appropriate to their particular organization. Although it is too early to evaluate the results for many of the programs described here, these programs show promise and should help other participants develop their default management plans.

This handbook also includes analyses based on the Department of Education's survey of student loan recipients. This survey provides us with new information on former GSL borrowers and thus enables us to ascertain who defaults and why.

The other information in this book is based on information provided by hundreds of officials of postsecondary institutions, guarantee agencies, state agencies, and major postsecondary education associations, from all 50 states and the District of Columbia. We discovered many organizations that are doing a remarkable job to reduce defaults. Space constraints prevented us from profiling every group we wanted to, but we have incorporated ideas from many groups in this handbook. We are grateful to all those people who took time to answer our questions and describe what their organizations are doing to reduce defaults.

Student loan defaults are a serious, but not an unsolvable, problem. By working together we can reduce defaults while increasing educational success for our students. Defaults are a waste of valuable student aid money and must be stopped.

Lauro F. Cavazos
Secretary of Education

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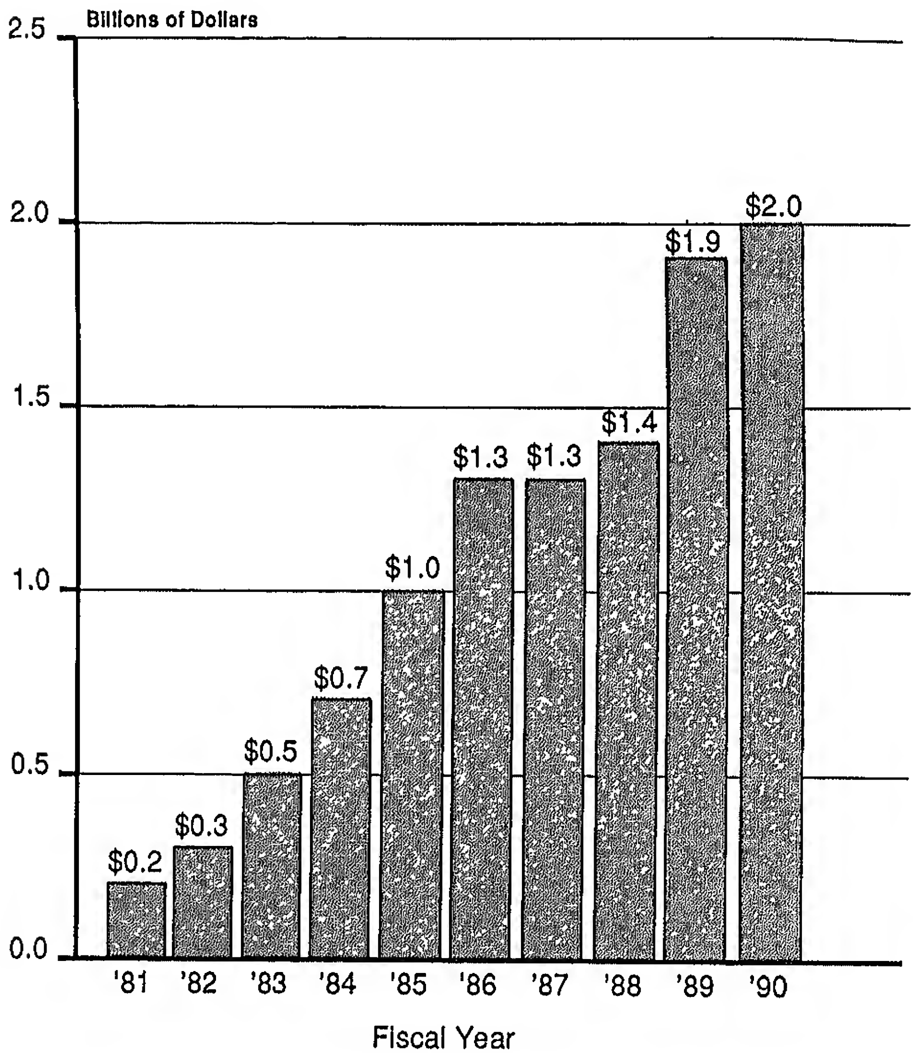
PART I

THE PROBLEM

Chart 1—The Annual Costs of Student Loan Defaults, Fiscal Year 1981–1990



Source: U.S. Department of Education, Office of Planning, Budget and Evaluation.

The Rising Cost of Student Loan Defaults

The high and increasing cost of defaults on federal student loans is a serious problem to everyone involved in postsecondary education today. The cumulative value of outstanding defaulted student loans will reach $7.8 billion in FY 1990. Default costs for FY 1989 alone were $1.9 billion, representing 44 percent of the total federal program expenditures. In FY 1990, default costs are expected to reach $2.0 billion (see Chart 1). This diversion of funds to pay bad debts places an unnecessary and wasteful demand on scarce federal resources—resources that could be used to aid current and future students.

Default costs have risen steadily in recent years largely because of an increase in loan volume. In FY 1990 an estimated $11 billion will be loaned to 4.1 million recipients in the GSL program, compared with $7.4 billion loaned to 3.4 million recipients in FY 1981.

But part of the increase in default costs is due to an increase in the percentage of borrowers who default. Loans entering repayment status grew from $2.3 billion in FY 1981 to $10.4 billion in FY 1990, a fourfold increase. Over the same period, however, default costs increased eightfold. If defaults were a separate program, it would be the fastest-growing program in the Department of Education today.

The Department of Education has expanded its collection efforts by increasing federal income tax refund offsets, federal employee salary offsets, referrals to the Department of Justice, and referrals to private collection services. Annual student loan default collections increased from $80 million in FY 1981 to an estimated $637 million in FY 1990.

Which Students Default

Recent Department of Education analyses show significant differences between the characteristics of defaulters and nondefaulters as shown in Table 1.

Table 1

Percentage of Defaulters and Nondefaulters Among Students Leaving Postsecondary Institutions in 1984 or 1985 by Selected Characteristics

Characteristic	*Defaulters*	*Nondefaulters*
Did not have a high school diploma	23%	6%
Did not have a high school diploma or a GED	9	2
Never earned a postsecondary degree or certificate	49	21
Earned less than $10,000 at time loan entered repayment status	51	24
Borrowed less than $2,500	70	44
Had only one loan	68	45
Attended a proprietary school	37	17
Had at least one dependent	47	27
Was separated or divorced	12	6
Was older than age 25 at time of enrollment	28	19

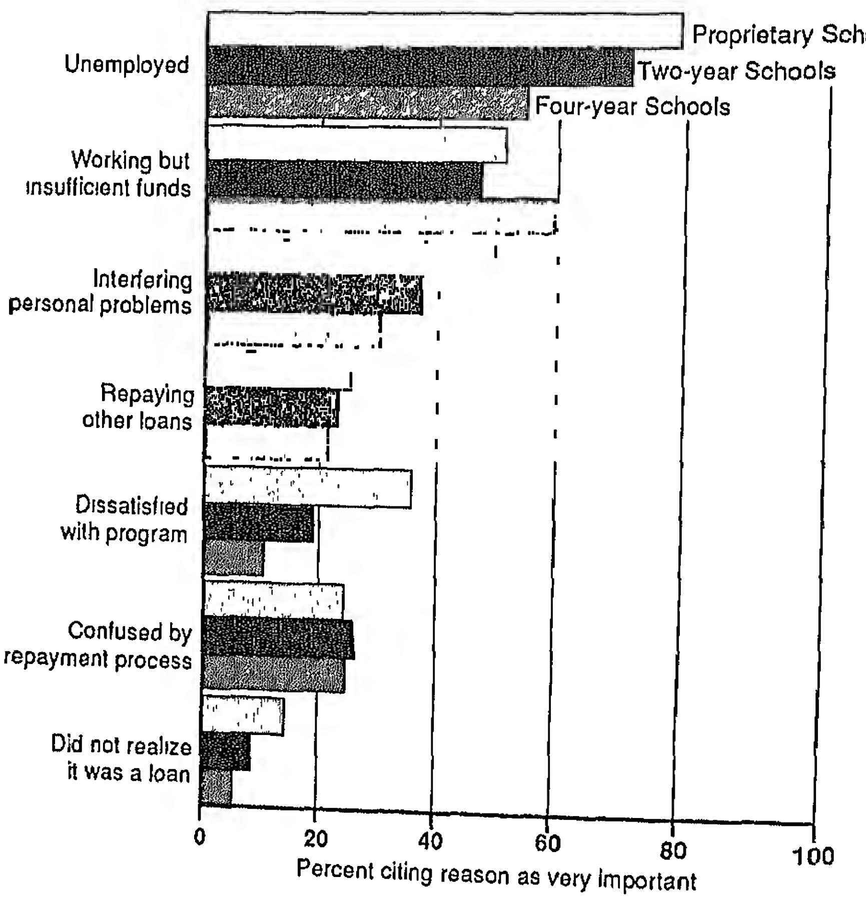
Source: U.S. Department of Education, 1987 National Postsecondary Student Aid Survey.

This analysis reveals the following:

- Defaulters were four times more likely than nondefaulters to enter their postsecondary education without a high school diploma. Of this group of defaulters, approximately 40 percent did not receive a general educational development certificate (GED).
- Defaulters were more than twice as likely to have dropped out of their postsecondary program.

- Defaulters were more than twice as likely to be unemployed or underemployed (earning less than $10,000) than nondefaulters at the time when repayment was scheduled to begin.
- Defaulters had fewer and smaller loans, which indicates that defaulters attended postsecondary institutions for fewer years or went to relatively inexpensive institutions. This statistic may be explained in part by the fact that a significantly larger percentage of defaulters than nondefaulters attended proprietary institutions—schools with programs usually lasting no more than two years.

Chart 2—Reasons Students Cited for Defaulting on Guaranteed Student Loans (Students Leaving Institution in 1984 or 1985)



Note: Some students gave multiple reasons for defaulting.
Source: U S. Department of Education, 1987 National Postsecondary Student Aid Survey.

Why Students Default

In 1986 the Department of Education asked a large group of defaulters to rate the relative importance of various circumstances in causing their default. The results, depicted in Chart 2 (and in parts of this graph which are reproduced throughout this handbook), indicate that most borrowers defaulted because they did not have, or did not believe they had, the ability to repay their loans. Many were also confused by the administrative loan process.

As the chart shows, "Unemployed and without income" was cited more often than any other reason. Defaulters ranked "Working but had insufficient funds" just below unemployment as a very important reason contributing to their default, and a significant number of defaulters said they were "Repaying more important loans than GSLs." All these circumstances detract from a borrower's financial ability to repay the loans.

These results also indicate that many borrowers are unaware of current repayment options available to them. Unemployed workers are allowed to defer loan repayments for up to two years, and employed borrowers who are willing but unable to meet their repayment schedule may request forbearance from their lenders.

Although a borrower's poor financial situation is the main factor in most defaults, other reasons also contribute to the problem. "Dissatisfaction with the education program" was cited as contributing to the default in 22 percent of all cases. This indicates the importance of a high-quality education, since some borrowers may not make loan payments if they believe they were cheated of a quality education. A surprisingly large percentage of defaulters, 39 percent, cited "Interfering personal problems."

Two other reasons cited, "Confused by repayment process" and "Did not realize loan had to be repaid," indicate the importance of loan counseling. A startling 10 percent of defaulters did not realize they had received a loan, which signals a lack of proper counseling by the postsecondary institutions and the lenders involved.

Chart 2 also shows that the reasons cited differ by institutional sector. Students who attended two-year and proprietary institutions tended to default because they were unemployed, whereas students who attended four-year institutions defaulted more often because they had insufficient funds, although they were working. Also, a greater percentage of proprietary school defaulters were unhappy with their school program than were students at other two-year and four-year institutions.

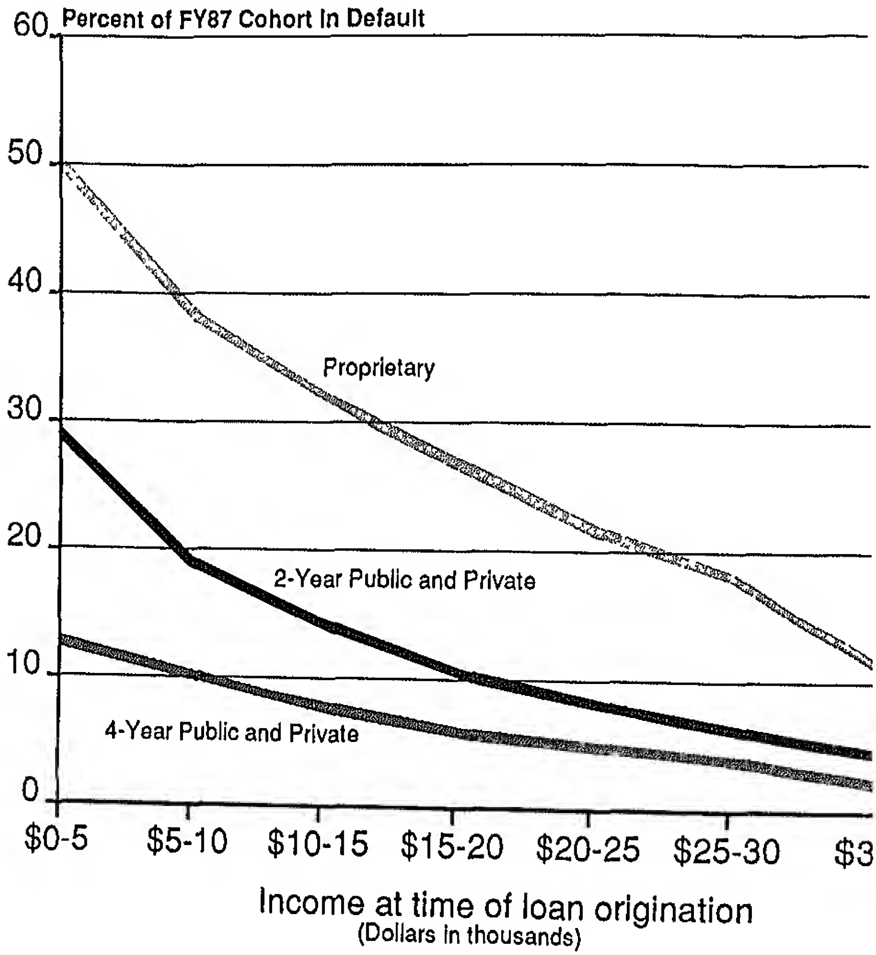
In summary, a more comprehensive effort must be made to prevent defaults from occurring: Increased counseling, especially on topics such as repayment options and student responsibilities, must be performed; students must be taught how to budget better their expenses; and administration of student loans

must be improved. Also, although student borrowers should be informed the loan deferment option in the event of unemployment, this type of defe ment is only a temporary solution. Borrowers need to gain the skills neces to find employment after graduation, and the institutions should be teachin those skills and helping with the job search

PART II

WHAT POSTSECONDARY INSTITUTIONS CAN DO

Chart 3—Stafford Loan Default Rates, by Family Income and Type of Institution



Source: U.S. Department of Education Office of Planning, Budget and Evaluation, based on data provided by the guarantee agencies.

Default and the Postsecondary Institution

When students first consider borrowing money to finance their education, often the first place they contact is the postsecondary institution. Therefore, these institutions are in a unique position to offer students advice, information, and referrals. They are also responsible for giving students a high-quality education, admitting and awarding aid only to students who can benefit from the institution's program, and helping the students find employment after completing the program. A high default rate for an institution suggests that the institution may not be meeting one or more of these responsibilities.

To evaluate the magnitude of each postsecondary institution's default problem and to require specific actions from high-default institutions, the Department of Education calculates a fiscal year cohort default rate—defined as the percentage of borrowers entering repayment status in one fiscal year who default before the end of the following fiscal year—for each school each year. The fiscal year 1987 cohort default rate for all institutions with at least 30 borrowers was 17 percent. This means that 17 percent of all borrowers who entered repayment status in FY 1987 defaulted before the end of FY 1988.

Table 2 shows that the average default rates for various institutional sectors differ significantly. For example, in FY 1987 proprietary schools had an average default rate of 33 percent—twice the rate of two-year institutions and more than four times the rate of four-year institutions. Also, proprietary schools, while accounting for 39 percent of the institutions participating in the student loan program, accounted for 89 percent of institutions with default rates greater than 60 percent and 84 percent of institutions with default rates greater than 40 percent.

Table 2
FY 1987 Cohort Default Rate by Type of Institution

Type of Institution	*Default Rate*
Proprietary	33%
Public two-year	18
Private two-year	14
Public four-year	7
Private four-year	7
All institutions	17

Source: U.S. Department of Education, Office of Planning, Budget and Evaluation, based on data provided by the guarantee agencies.

Although proprietary schools do enroll students with the lowest incomes, Chart 3 shows that proprietary schools in FY 1987 had higher default rates than other institutions across all family income ranges. This comparison provides evidence that proprietary schools can do more to reduce their defaults. In fact, many proprietary schools enroll low-income students and have low default rates.

But not all high-default institutions are proprietary schools. Thirty percent c two-year institutions and 6 percent of four-year institutions had default rates greater than 20 percent—a rate that can be reduced with stronger action. Th default problem is not simply a proprietary school problem; it exists for all i stitutions.

Recommendation #1
Counsel all students on their loan responsibilities.

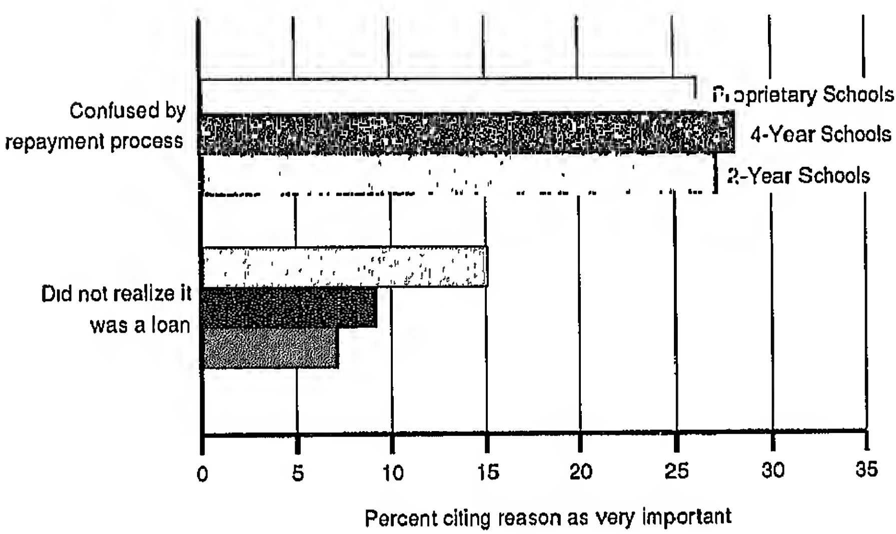
A Department of Education study shows that many defaulters are confused about the loan process and their repayment responsibilities (see Chart 4). Postsecondary institutions are now required to counsel students before disbursing funds (at entrance) and again before students leave the school (at exit). These counseling sessions give the institution an opportunity to improve borrowers' understanding of the terms and conditions of the loans and impress on all borrowers the importance of meeting their repayment obligations.

Entrance Counseling

Students must understand the responsibilities and the debt burden they will face *before* they take out a loan. Also, the entrance interview may be the only opportunity the school has to communicate with students who withdraw on little or no notice. Thus, all aspects of the Guaranteed Student Loan programs must be covered during this initial counseling session. The school should—

—emphasize that borrowers must repay their loans even if they do not complete the program or believe they benefited from the program;

Chart 4—Reason for Defaulting on GSL: Lack of Adequate Counseling



Source: See Chart 2.

—discuss the terms and conditions of GSL loans;

—review the student's rights and responsibilities, the ramifications of default, and the repayment options available to borrowers (see Appendix A through E);

—encourage students to borrow the minimum amount needed, thus reducing borrowers' monthly payments;

—provide a sample repayment table that presents average anticipated monthly repayment based on projected indebtedness (see Appendix C);

—help students to understand the sale of loans by lenders and the use by lenders of outside contractors to service loans; and

—collect additional information from borrowers, such as names of their next-of-kin and Social Security and driver's license numbers, to help lenders in locating the borrowers if necessary.

Many institutions have found that giving students a written test following the counseling session is especially effective for measuring the students' comprehension of the topics discussed in the meeting. Intensive counseling should follow for students who fail. The test could include—

—the stated interest rate on the borrower's loan,

—the applicable grace period provided to the borrower and the approximate date the first installment payment will be due,

—a description of the charges that may be imposed on delinquent payments,

—consequences of default,

—key student responsibilities,

—repayment options, and

—financial terms that are necessary for borrowers to know (e.g., loan servicer, grace period, interest capitalization).

Exit Counseling

Immediately before a student leaves school or after a school learns that a student has dropped out, a counselor should contact the student and schedule an exit interview. This session should reiterate the student's rights and responsibilities, the terms and conditions of the loans, ramifications of default, and repayment options, and also emphasize the actions the student will need to take in the months ahead. In addition, the school should—

—provide a sample loan repayment schedule based on the borrower's total loan indebtedness for attendance at that institution;

—provide the name and address of the borrower's lender(s) according to the institution's records;

—provide guidance on the preparation of correspondence to the borrower's lender(s) and completion of deferment forms (perhaps including sample letters and change of address notices that the student might send to lenders);

—review the role of loan servicers and secondary markets;

—obtain information regarding the borrower's address, the address of the borrower's next-of-kin, and the name and address of the borrower's expected employer;

—suggest to the borrower some debt management strategies to facilitate repayment by the borrower; and

—strongly encourage borrowers who have any questions to seek help from their institution, their lender or loan servicer, or the Federal Student Information Center (1-800-333-INFO).

COUNSELING STUDENTS: Court Reporting Institute of Dallas Dallas, Texas

The Court Reporting Institute of Dallas (CRID), the largest court reporting school in the country, has developed a comprehensive counseling program. In addition to requiring students to attend entrance and exit interview sessions, CRID also reminds students of their loan responsibilities when they pick up the second disbursement of their loans and holds an annual default prevention week.

With this latter action, CRID has managed to make default counseling not only informative but entertaining. Two years ago, CRID decided to designate one week of every school year as Default Prevention Week, during which activities and events designed to increase students' awareness of student loans would be incorporated into the regular class schedule. In 1989 CRID chose the theme Default Busters (inspired by the movie *Ghostbusters*). The week's activities included the following:

- *School-wide awareness campaign.* Students were given Default Buster buttons, and those who were wearing buttons when their names were called were awarded prizes.
- *Panel discussion.* This focused on the roles of the borrower, school, lender, servicer, and guarantor in the loan and repayment processes, featuring the head of the local guarantee agency, a representative from the regional office of the U.S. Department of Education, a representative from a local lender, and a representative from the local servicer. The discussion was followed by a question and answer period.
- *Student loan I.Q. test.* Students studied information provided on a student loan fact sheet and took a written exam at the end of the day. Throughout the week a person designated as the Default Buster visited classrooms to quiz the students orally on questions randomly selected from the I.Q. test. Students who answered correctly received steno paper, and those who answered incorrectly were slimed by a ping pong gun.
- *Theme design contest.* Students this year were invited to design creative T-shirts; the top three designers won cash prizes of $500, $100, and $50. The T-shirts were sent to state legislators. Last year CRID held a poster design contest.
- *Letter writing campaign.* Students wrote to state and federal legislators thanking them for supporting the GSL program and thus enabling them to receive an education, describing their future plans, and informing them of their intention to repay their loans.

- *Entertaining final presentation* including a skit and a music rap performed by CRID's faculty and staff. This year's skit, CRID's adaptation of the Three Little Pigs, demonstrated the detrimental, long-term effects of failing to repay loans.[1]

1 The first two pigs who had defaulted on their loans were rejected for a housing loan and were forced to build their homes using sticks and straws. The third pig, who had repaid his loan, received a mortgage and was able to build his home with bricks. The wolf, alias Fed. Gov., was able to blow down only the homes of the first two pigs. After experiencing loss of credit, the first two pigs made arrangements to repay their student loans.

COUNSELING STUDENTS:
Spelman College
Atlanta, Georgia

Spelman College, founded in 1881, is a historically black women's college in Atlanta, Georgia, with an enrollment of about 1,800 students. It offers a liberal arts education in a supportive learning environment, which extends to the financial aid counseling program. Spelman's program involves not only students but also the families of students, and it starts not when the students begin college, but from the time young people begin thinking about college. Spelman's counseling program involves many steps:

- Staff from Spelman's financial aid office visit high schools and churches upon request to discuss financial aid options with high school juniors and seniors.
- When prospective students and their parents come to visit Spelman, the financial aid office gives them information about loans, emphasizing the seriousness of debt and the students' responsibilities.
- Once admitted to Spelman, students are required to meet with financial aid officers on a one-on-one basis at least twice a year. Topics of discussion include debt management, expected repayment, interest rates, and loan consolidation. During the counseling session, the students' financial records are discussed and staff strongly advise students to borrow the smallest amount necessary.
- If a student chooses to leave Spelman before graduating or is dismissed from the college, counseling services are provided concerning financial aid and the responsibility of loan repayment.

ɔmmendation #2
·k closely with lenders to
ıce defaults.

ındary institutions and lenders both are concerned about defaults. fault institutions may not be allowed to participate in the student loan , and high-default lenders lose time and money collecting on delin- ans. By sharing information, ideas, and responsibilities, both schools lers stand to benefit from lower default rates.

forge a cooperative relationship, schools should take the following ac-

Meet with representatives from the lending institutions and learn about the actions lenders are taking to reduce defaults.

Recommend responsible lenders to students.

Coordinate efforts to ensure that students will receive counseling on all relevant aspects of repayment. For example, some postsecondary institutions that do not have the staff to counsel students on personal financial planning enlist the lender to counsel students on this topic.

Provide lenders with pertinent information on the student's whereabouts, such as references, possible employers from placement files, name changes, social security number, and driver's license number.

Notify the lender when a student's enrollment status changes. The sooner the lender knows that a student has left school, the easier it will be to locate the person and establish a repayment schedule.

Contact the lender when the institution cannot locate a student. This will allow banks to begin skip tracing, to locate the student as soon as possible.

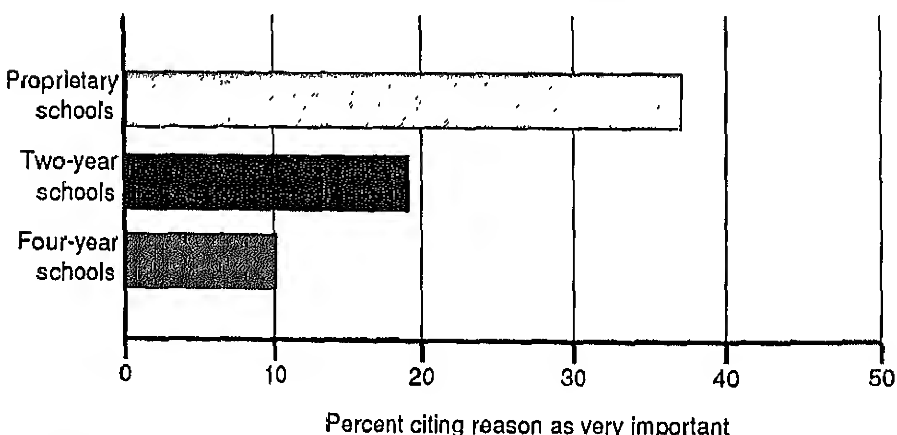
Recommendation #3
Improve the quality of the education offered at the institution.

An institution that offers a high-quality education will ensure that its students have the necessary skills to find employment and meet their financial responsibilities after they graduate. Also, as Chart 5 shows, some students default because they are unhappy with the education they received.

Institutions must meet the challenge of offering their students the highest-quality education in the following ways:

- *Strengthening the curriculum.* The curriculum offered should be up-to-date, comprehensive, and challenging. For example, a secretarial school should teach more than typing and dictation; it should teach writing, office management, and basic computer skills.
- *Insisting on an excellent faculty.* The faculty must have good qualifications, and the faculty should be large enough to give students individual attention. By evaluating faculty periodically, schools can improve or replace poorly qualified staff and hire additional personnel when the need arises.
- *Improving the availability and effectiveness of academic counseling.* One-to-one tutoring can be very effective in assisting students in their coursework.
- *Updating facilities, materials, and equipment.* Teaching students how to handle antiquated machinery or to program in an obsolete computer language will not prepare students adequately for jobs in today's market.

Chart 5—Reason for Defaulting on GSL: Dissatisfied with Program



urce: See Chart 2.

Recommendation #4
Improve retention programs to keep students in school.

Half of all defaulters drop out before completing their postsecondary education. Many who drop out are ill-equipped to find employment later and do not have the means to repay their loans; others quit school because they were dissatisfied with the program and refuse to repay because they feel cheated. An institution that has a high dropout rate should develop and implement a comprehensive program to attack the attrition problem. In implementing a program, schools should take the following actions:

- *Strengthen the academic counseling program.* A school can hire more tutors, require the faculty to serve as academic advisers, and offer remedial classes.
- *Revise the admissions policy and screening practices to ensure that students enrolled in the institution have a reasonable expectation of succeeding in their programs of study.* One way to determine whether students will be able to complete the program is to require potential students to pass an exam designed to test their skills and educational background.
- *Use only salaried employees or volunteers to recruit students.* Studies on proprietary institutions have found many examples of aggressive, commissioned representatives or salespeople who used misleading information and exaggerated promises to recruit students.[1]
- *Provide accurate information concerning completion rates, cost of attendance, and program requirements* so students can assess their chance of completing the program before committing themselves to the program or to a student loan. This action is now required of all nonbaccalaureate vocational programs.

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1 Pelavin Associates, Inc., *Consumer Rights and Accountability in Postsecondary Vocational-Technical Education: An Exploratory Study*, 1988; Interface, *Unfair At Any Price: Welfare Recipients At New York Proprietary Schools*, 1989.

IMPROVING STUDENT RETENTION:
Valley College of Medical and Dental Careers
Los Angeles, California

Valley College of Medical and Dental Careers, located in an inner-city neighborhood of Los Angeles, enrolls 650 students, approximately three-quarters of whom are from disadvantaged or low-income backgrounds. Because of the financial and academic difficulties its students face, Valley College developed a program in 1987 to help its students stay in school, eventually graduate, and become medical and dental professionals.

Valley College's student retention program has several features:

- *The admissions procedure* includes testing designed to admit only those students who will benefit from the program. This policy, however, does not discriminate against the poor. For example, the school accepted one student who was homeless at the time of her entrance interview; she graduated recently and now has a job paying $20 an hour.
- *Academic tutoring* helps students keep up in their coursework. The main difficulty for most students is in mathematics, so Valley College has implemented special math classes to improve students' math skills. The college also established the Lamplighting Program, a peer-tutoring program in which student tutors, or lamplighters, as they are called, help their peers with any academic problems.
- *Student Services*, a new Valley College program, helps students deal with problems outside school that often affect students' performance in school. For example, one female student who was being physically abused by her husband was directed to a crisis intervention agency and placed in a safe house; she was then able to complete her education. Student Services also helps students find carpools, volunteer opportunities in the health care area, and part-time jobs.
- *Students' absences are monitored.* If a student is absent one day, the teacher calls the student at home to find out the reason for the absence. If the student is absent for two days, the teacher and another staff person call. The monitoring continues until the student returns.

Valley College reports that its retention rate has increased 30 percent since the program began.

Recommendation #5
Work to reduce defaults by dropouts.

Students who drop out of a program default on their loans at a much higher rate than do students who graduate. Many withdrawals occur during the first two weeks of classes, before the students have put substantial time and effort into their coursework. Students who drop out during this initial period are sometimes held responsible for the entire tuition charged for the school session. By not disbursing student loan funds to students during the first 30 days of enrollment and by giving students who drop out after 30 days a fair refund for the balance of the session, postsecondary institutions can reduce default costs due to withdrawals. Here are some specific actions these institutions can take:

- Delay certification of first-time borrowers' loan applications so that the borrowers receive no loan proceeds until at least 30 days into the loan period. Currently, schools with default rates greater than 30 percent are required to delay certification for first-time borrowers; and all schools, regardless of default rate, are required to delay certification of SLS loans for first-time borrowers.
- Be aware of problem signs, such as a series of absences. If students seem to be having problems with the coursework, encourage them to receive academic or other counseling.
- Increase the review of students' in-school status so as to recognize promptly those instances in which borrowers withdraw without notifying the institution. The sooner the school and lender know that a student has left school, the easier it will be to track the former student's whereabouts when repayment is due.
- Explain carefully to prospective students that if they are dissatisfied with the education or do not complete the school session, they will still be held responsible for repaying the loan.
- Establish a fair and equitable refund policy. One considered fair is a pro-rata refund policy, which is currently required of schools with default rates greater than 30 percent. Whatever their refund policy, schools should clearly state their refund policy to all students before they receive a loan.
- Process refunds quickly.
- When the lender is sent a refund to be applied to the student loan, send a notice to the student telling him to contact the lender immediately to begin repaying the balance.

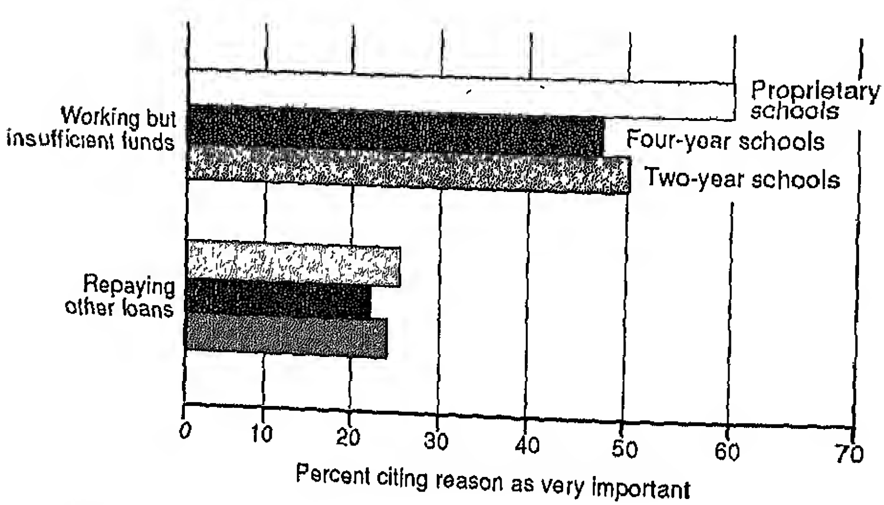
Recommendation #6
Teach students to budget and manage their personal finances.

Too many students default because they cannot budget their finances. A significant number of former students, even though they were working, did not have the funds available to repay their loans—or they were repaying other loans (see Chart 6).

Students often blindly accept student loans without understanding the financial burden that loans will place on their economic situation after they leave school. The jobs they are offered immediately after graduation will often be entry-level positions, and the deduction of taxes and insurance from their salary could leave very little to pay all their living expenses as well as their student loan(s).

To determine how much money they need to borrow and how much they will be able to repay after graduation, potential borrowers need to calculate their in-school and out-of-school budgets. Schools can help students by offering courses in budgeting and personal financial management or by including this type of material in the entrance and exit counseling sessions. Some institutions have found it helpful to work with bankers and insurance representatives to develop a course outline and present the material.

Chart 6—Reason for Defaulting on GSL: Difficulty Budgeting Finances



ource: See Chart 2.

In the budget session, the instructor should—

—help students realistically assess their finances;

—emphasize the danger of excessive indebtedness because bad credit can be very detrimental to borrowers in future years;

—advise students of their options if repayment is impossible;

—emphasize the need to begin detailed financial planning while in the grace period (repayment will be due six months after graduation); and

—inform students of the option to consolidate loans for more manageable payments.

The session can be divided into two parts, covering the in-school budget and the out-of-school budget. Appendix D contains samples of both budget worksheets.

TEACHING STUDENTS TO BUDGET: ***St. John's University New York, New York***

St John's University, a Catholic university founded by the Vincentian Fathers in 1870, is located in New York City and has two campuses, one in Queens and the other on Staten Island. Forty percent of the students who apply for financial aid come from families with incomes under $30,000.

St. John's University has no dormitory facilities, so students must seek off-campus housing, which tends to be costly. To help its students budget expenses while in school and make their financial plans for the future, the University started a Financial Planning and Debt Management program five years ago. It includes the following features:

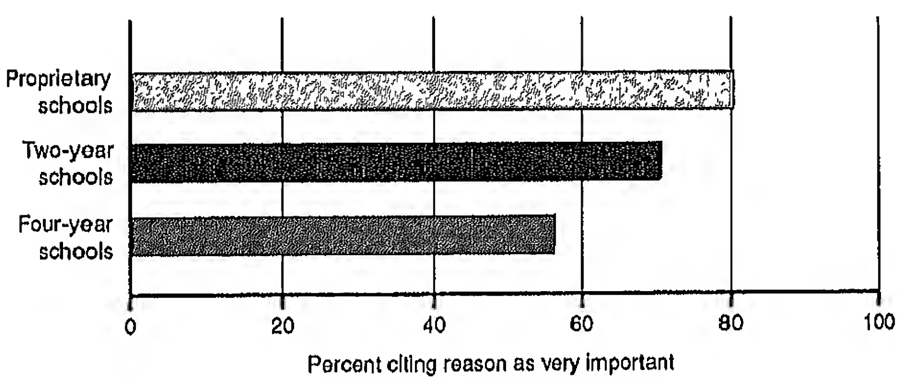
- St. John's University conducts financial planning and debt management seminars during freshman orientation sessions and at least once each semester These seminars are usually held during the University's activity hour, when no classes are scheduled.
- To encourage students to attend these seminars, the financial aid office mails flyers advertising the seminar to all students receiving financial aid, and mails letters to faculty members asking for their help in persuading students to attend.
- Seminars usually lead off with a discussion of loan indebtedness and proceed with topics such as credit management, investments, and money management. Local bank representatives and faculty members are often invited to make presentations in these seminars.
- The University developed a set of brochures for undergraduate, graduate, and law students that contain (1) worksheets to help students budget their money while in school and after they graduate, (2) the employment outlook for 1986 to 2000 from the spring issue of the *Occupational Outlook Quarterly*, (3) information about the average starting salaries of St. John's graduates by academic major, and (4) repayment schedules.
- The University developed a guide for other institutions that outlines its financial planning and debt management initiative. This guide has been sent to all colleges, universities and proprietary institutions that are members of a national student aid association (NASFAA).

Recommendation #7
Establish a good job placement program.

The most common reason borrowers default is that they are unemployed (see Chart 7). Schools with low job placement rates must make job placement a real priority. To do this they can take the following steps:

- Increase contacts with local employers by inviting companies to recruit on campus or by holding job fairs where potential employers can speak with students.
- Establish a job placement center where students can go to obtain counseling, information about potential employers, and information on job search strategies. Many schools have centers where students can learn how to handle interviews effectively and how to compose persuasive resumes and cover letters.
- Ensure that the job placement center has the staff necessary to work with students during their first year of school and help them think about, prepare for, and eventually search for employment.
- Explore with local employers the feasibility of establishing internship and cooperative education programs.
- Work with the local office of the U.S. Employment Service and the Private Industry Council supported by the U.S. Department of Labor to obtain job information and placement assistance for students.
- Establish or improve an alumni network through which alumni can meet with students to offer advice, information, and job leads.

Chart 7—Reason for Defaulting on GSL: Unemployed



Source: See Chart 2.

HELPING STUDENTS FIND JOBS: Baker College of Business Flint, Michigan

Baker College of Business, a private non-profit school with campuses in Flint, Muskegon, and Owosso, Michigan, offers two- and four-year programs in a wide range of fields. Primarily a career college serving adults who are returning to education, most of the school's students range in age from 21 to 40 and already have some work experience before attending. Baker College often provides training to people seeking a career change after being laid off in other industries.

Baker College recognizes the value of actual work experience, both to enhance what students learn in the classroom and to increase employment opportunities upon graduation. Through work, students also learn valuable job skills, including handling responsibility and getting along with employers.

The school sponsors two work-experience programs that allow students to get on-the-job experience with preparation for work in their chosen fields. More than 60 percent of the graduating students participate in one of the two work-experience programs offered at Baker College.

- The Co-op Program allows students to earn four class credits and a regular salary for part-time work after school and on weekends. Students usually begin working in the last or next-to-last quarter of school. The program matches employers and students in fields such as business management, computer programming, and travel and tourism planning. Many students find that the Co-op Program leads to permanent employment at the firm where they interned while in school.
- The second internship, also worth four class credits, requires between 120 and 300 hours of work over a 10- to 12-week period and is required for graduation in several of the programs. For example, participation is required in biomedical technology, statistical process control, drafting, and roughly 10 other fields of the 33 associate degrees offered at Baker College. This program is generally shorter than a Co-op internship and is unpaid. The requirement makes graduates of these programs attractive to prospective employers who know that the school is providing them with well-trained and experienced personnel.

According to Baker College, approximately 20 percent of its graduates get jobs from their work-experience employers.

Baker College supplements the two internships with a seminar in employment strategies. Students are required to successfully complete the seminar in order to graduate. The seminar is a two-day, eight-hour course that teaches students

interviewing techniques and resume writing. Teachers also define application procedures, explain ways of evaluating different job offers, and suggest dress and appearance choices.

Baker College's job placement office is run by four full-time staff members. In combination with the two internship programs, the office's efforts result in the placement of almost half the school's graduates. The office arranges much of the contact between students and potential employers, including presentations, on-campus interviews, mailings, and even breakfasts with company officials.

Baker College claims to have an overall employment rate of approximately 96 percent among its graduates.

Recommendation #8
Keep in touch with borrowers after they leave school.

The first year after a student leaves the institution is critical. Often the former students have not yet found jobs, or jobs that meet their expectations, and they have incurred many new financial responsibilities. They may have moved recently and not given their lender their new address; or they may not have received a bill from their lender and may not realize that they are responsible for making a payment anyway. During this period, educational institutions should play a supportive role while still ensuring that borrowers do not enter default. Institutions should take the following actions:

- Send follow-up letters and make phone calls to remind former students when their loan payments are due.
- Encourage former students to call the institution if they have any questions.
- Invite former students to make an appointment with a counselor if they are having a problem with payments. Inform former students of the options they have if repayment is impossible.
- Encourage unemployed former students to use the job placement services at the institution.
- Use skip tracing to locate former students if necessary. Once the former students have been found, check to be sure they are making timely payments.

WORKING WITH FORMER STUDENTS:
Phoenix Institute of Technology
Phoenix, Arizona

In 1986, Phoenix Institute of Technology (PIT), which offers courses in electronic technology, automotive technology, and drafting and commercial art, began a comprehensive program to reduce its loan default rate. It incorporated many elements into its plan—counseling students about loans, teaching them about budgeting, working to keep them in school, and tutoring them for the GED.

In addition, PIT continues to assist borrowers after they leave the institution. This includes two features:

- *Delinquency and default lists.* PIT checks the delinquency and default lists provided by the lender and guarantee agency and attempts to contact former students who are not repaying their loans, first by letter and then, if necessary, by telephone. The letters remind former students of their obligations to repay their loans and the possibility of deferment or forbearance in some cases. The letters also warn of the many serious consequences of default and the need for borrowers to remain in contact with their lenders. If telephone contact is successfully made with a borrower or a reference, an update of the borrower's address and telephone number is requested and the borrower is strongly urged to contact the lender.
- *Placement office.* The placement office continues to be involved after students graduate. When the office gets a request for placement assistance, former students who are still in the grace period are sent employment information and a reminder about loans coming due. The placement office is also notified when a graduate becomes delinquent or is in default. Borrowers in delinquent or default status are advised to begin repaying their loans.

Recommendation #9
Analyze the default problem at the institution and take the appropriate actions.

To determine where most effort is needed, each institution should determine the causes of default by its students. To answer the question, "Why do our students default?" each institution can collect and analyze the following information:

- the job placement rate for former students,
- the employment rate in students' fields of study (for career and vocational schools),
- the dropout rate,
- the certification rate and licensure rate (for career and vocational schools), and
- the reasons former students give for defaulting.

An institution that has a low job placement rate should strengthen its job placement program and update its curriculum so that students will have the skills necessary to join the job market.

An institution that has a high dropout rate must determine why students are not staying in the program. Are they inadequately prepared for the program? Once in the program are they not receiving academic tutoring and counseling? Did students have unrealistic expectations about the program? Were the students not serious about completing the program from the start? An institution can make changes to the admissions policy and the curriculum to ensure that students who are admitted will stay in the program. Schools can also take certain precautions, such as delaying disbursement of loan funds,[1] so that students who do drop out early do not owe large amounts of student loan funds.

An institution that has low certification and licensure rates may not be providing adequate training to its students. The institution should make an extra effort to determine which skills and knowledge are necessary to pass certification and licensing examinations and include courses in its curriculum to address these needs.

An institution whose students are graduating from the program, being certified and licensed (if the institution is a professional school), and getting sufficiently high-paying jobs must look deeper to determine why its students default. Former students who defaulted can be interviewed. Did they understand the

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[1] Currently, all schools must delay disbursement of SLS funds and high-default schools must delay disbursement of GSL funds to first-time borrowers for 30 days.

fications of defaulting? If not, this problem should be more heavily em-
ized in the counseling session for future loan recipients. Were the defaul-
ıaving problems making ends meet each month? If so, a budgeting and
umer course could be developed. Were the defaulters not repaying their
s because of administrative misunderstanding and confusion with their
ers? If so, the institution could arrange a meeting with area lenders to dis-
the problems students are encountering. Lenders who attempt to com-
icate with their borrowers and diligently collect loans could be
mmended to future students.

pproach to default reduction that works at one institution may not be the
approach for another institution. Each must tailor a plan for reducing
ults that meets its needs and situation.

ANALYZING THE DEFAULT PROBLEM:
Al Collins Graphic Design School
Tempe, Arizona

Al Collins Graphic Design School in Tempe, Arizona, trains students to be commercial artists and illustrators. In January 1988, Al Collins hired a full-time loan default manager, Mary Lyn Hammer, to help the school lower its default rate. By listening to the students and investigating their claims, Hammer discovered that most defaults resulted from a lack of communication among the students, lenders, servicers, guarantors, and secondary markets, or from the students' dropping out of school.

To deal with the first problem, the school authorized Mary Lyn Hammer to—

—resolve problems with lenders;

—help students apply for deferment of repayment or forbearance;

—help students get affordable payments by cross-referencing loans sold to different secondary markets;

—maintain a data base on all loan recipients. This includes current status, enrollment dates, current address and phone number, employment information, emergency contacts and other references, loan repayment schedules, lenders, servicers, secondary market holders, guarantors of the loans, and account activity data;

—help borrowers get out of delinquent status (based on reports provided by the lenders);

—conduct automatic skip tracing when an address is no longer valid or when requested by a lender or servicer; and

—provide monthly separation reports to lenders (i.e., monthly listings of the lender's student borrowers along with the school's most current information on each student, such as last date of attendance, current address, phone number, reference data, and employment data).

To deal with the second problem—students' dropping out—the school developed a retention program, consisting of the following activities:

- The school closely monitors students' attendance.
- A student who indicates an intention to drop out, or who has an attendance record or grades close to minimum standards, is required to meet with a group of administrators and faculty who counsel students individually to improve their situations.
- The school sends several letters to dropouts, reminding them of their repayment obligations and options and encouraging them to return to school.
- Some students who are having financial difficulties are encouraged to switch to the evening program rather than drop out.

PART III

WHAT LENDERS CAN DO

Default and the Lender

In a recent study of lenders and defaults conducted for the Department of Education,[1] researchers concluded that neither the income of the borrower at the time of loan origination nor the type of school the borrower attended is the sole indicator of a high lender default rate. Table 3 shows that lenders with high default rates tend to have higher-than-average default rates across all sectors of postsecondary institutions. This suggests that borrowers' repayment performance may be related to lenders' practices.

Table 3
Average Fiscal Year 1985 Cohort Default Rate by Sector for High-Default and Low-Default Lenders[2]
(largest 100 institutions)

Type of Institution	*High-Default Lenders*	*Low-Default Lenders*
Private two-year	26.9%	5.9%
Public two-year	35.9	9.5
Private four-year	17.8	5.1
Public four-year	17.7	4.6
Proprietary	44.6	13.1

Source: Federal Funds Information for States.

An earlier study, conducted in 1986 for the Department of Education,[3] identified several activities that significantly lower the lenders' default rates:

- Multiple disbursing of loans throughout the school year.
- Contacting borrowers directly to update their status while they are in school.

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1 Federal Funds Information for States, *An Analysis of Lender Default Rates in the Stafford Loan Program*, June 1989.

2 High-default lenders had rates of above 30 percent and low-default lenders had rates below 10 percent.

3 Applied Management Sciences, Inc., *A Demonstration of Behavior Scoring Models to Prevent Defaults and to Collect Defaulted Loans in the Guaranteed Student Loan Program*, 1986.

- Conducting enrollment verification from the borrower's institution.
- Verifying academic progress from the borrower's institution.
- Reporting loan approvals to credit bureaus.

The first four activities provide lenders with current information on each borrower's enrollment, academic progress, address, and anticipated graduation date. This information is important not only because it helps lenders locate borrowers more quickly after they leave the institution, but also because it allows lenders to identify dropouts early and put them into repayment status. Multiple disbursement also leads to a reduced loan amount for dropouts, possibly making payments more affordable.

The last activity, reporting loan approvals to credit bureaus, if communicated to borrowers, can impress on them the fact that failure to repay will impair their credit ratings.

The study also found that lenders with specific divisions or account representatives to handle student loans were more successful than others in preventing delinquent cases from becoming more delinquent or from defaulting. The servicing of student loans is very different from the servicing of commercial or other personal loans. Having staff with expertise and experience in working with student loans has been found to help significantly in collections.

In summary, strong actions by a lender—actions taken while students are in school and after they enter repayment status—can reduce the lender's default rate.

Recommendation #1
Research the loan risk before lending money.

Lenders are allowed to—and should—research the loan risk before offering a student a loan. This research involves evaluating the student's credit history and the institution.

- *Check the student's credit history; if it is poor, require a cosigner.*

  Every lender checks a potential borrower's credit history before making a private loan; the same should apply for student loans. Students often have no credit history, and they should not be discriminated against for lack of a history; but a lender should check with national credit bureaus to determine whether the student has unpaid or delinquent debt. If a student has such a poor credit history, the lender should require a cosigner.

- *Evaluate the postsecondary institution the student will be attending.*

  Lenders should evaluate the institution the student will attend—including its default, job placement, program completion, professional certification and licensure rates. If the evaluation is unsatisfactory, the lender should not lend the student money to attend this particular school. The lender should explain why it will not offer the student a Guaranteed Student Loan to attend that particular institution and advise the student that a loan would be available to attend another school.

Recommendation #2
Communicate effectively with student borrowers during all phases of the loan process.

Studies have found that students who had been in touch with their lenders before the repayment period began were less likely to default. Studies have also found that borrowers who default usually never made the first payment.[1] Lenders must make every effort to get the student to make that critical first payment.

In doing this, it is important for lenders to remember that student loans are often the first major debt that students will incur. Interest capitalization, forbearance, loan servicers, and insurance and origination fees are terms that are completely foreign to many borrowers. Any communication with borrowers should be conducted in plain language and any unfamiliar terms should be carefully explained.

To communicate effectively with borrowers, lenders should take the following steps:

- Counsel students before lending money to ensure they understand their responsibilities, the debt burden they will have after graduation, and the consequences of default.
- Encourage borrowers to visit or call the loan office when they have questions, need information, or have problems with repayment.
- Promptly notify the borrower if they sell the loan, informing the borrower of the new lender and the new address to which loan payments must be sent.
- Write all correspondence in terms that borrowers can easily understand.
- Coordinate efforts with schools and help them counsel students.

1 Career Training Foundation, *Default Management Manual*, 1987.

COMMUNICATING WITH BORROWERS: Citibank Southwestern United States

The Citibank Student Loan Business has a number of Account Managers who visit postsecondary institutions in the country. Jim Roth is an Account Manager for the Southwest Region who has addressed a number of student groups on the subject of their future financial responsibilities. The atmosphere is both instructive and supportive; students listen and are encouraged to participate.

During these sessions, the Citibank Account Manager helps students preview their first year out of school. A scenario is presented depicting a graduate with a job paying $20,000 a year. Questions of "How much will you be required to pay for rent?"; "How much will a car cost you?"; "How about clothes?"; etc. are asked. Using the responses from the students, Roth is able to illustrate to students that it will be difficult, even with a good job, to cover all their anticipated expenses and still pay off their student loans.

Roth then asks students to consider and propose alternatives to an expensive lifestyle. The students typically make suggestions like: "You could get a roommate"; "You could move back home." All offered suggestions are discussed. The students begin to feel the implications of their debt at this point.

The Account Manager then points out that their first loan payments will be due six months after they graduate. Students are asked to envision what that time will be like. If the students are enrolled in a typical college or university, they are reminded that it will be around the holiday season. They will want to spend money on gifts and other holiday expenses. Therefore, they are encouraged to save some money during the grace period to help prepare themselves to meet their first payment obligation and still enjoy the holiday season.

Roth also strongly encourages students to contact their lenders if they have trouble paying back their loans. It is made clear that most banks would "much rather have a student go into a restructured payment program than lose [the student to default]." They are told plainly "Do not duck out [of paying off your loans], because someone will find you."

Students pay attention to the presentation by Roth, or one of his fellow Account Managers, because they realize he is a banker who deals with these issues on a daily basis.

COMMUNICATING WITH BORROWERS: Signet Bank Baltimore, Maryland

Signet Bank, Maryland's lender of last resort and lender to nearly 50,000 students nationwide, has recently implemented a new program to make sure that students who take out Guaranteed Student Loans understand that they have borrowed the money from a bank and must repay the bank.

In 1989 the bank surveyed students from one high-default postsecondary institution in Maryland and discovered that some students who borrowed money from Signet did not understand that their financial assistance was a loan and not a grant. The survey also found that 10 percent of the borrowers had dropped out of the institution and that 6 percent had not filled out their own loan applications. In addition, one-quarter of the loan applications contained incorrect information.

Signet found that many institutions filled out loan applications for their students and simply asked the students to sign on the bottom line. Thus, many students did not understand that the applications originate at a bank, are processed by a bank, and result in an agreement with a bank to repay the loan after graduation.

As a result of its survey findings, Signet now requires students at high-default institutions to obtain loan applications from the bank instead of the educational institution. On September 25, 1989, Signet sent a letter to 26 postsecondary institutions in Maryland, each of which had default rates exceeding 25 percent, explaining that these institutions would no longer receive loan applications from the bank and that students who attended these institutions should contact the bank directly for applications.

Forcing students to contact the bank to apply for a loan instead of going to their financial aid office will make students aware of the relationship between the borrower and the lending institution.

Recommendation #3
Use effective collection techniques.

According to the National Postsecondary Student Aid Study (NPSAS), 27 percent of defaulters reported that they were confused by the repayment process. They were wrongly billed, never contacted for repayment, or had other problems with the lender.

Once student borrowers enter repayment status, lenders bear the immediate responsibility for ensuring that students do not enter default. To ensure that lenders meet this requirement, the Department of Education requires lenders to perform due-diligence procedures in loan collections when loans become delinquent to get the loan back into repayment. Due-diligence procedures consist of the following steps:

- When a loan is delinquent, the lender must send the borrower at least two collection notices during the first 30 days.
- When a loan is delinquent by 31 to 60 days, the lender must attempt to contact the borrower twice by telephone.
- When a loan is delinquent by 61 to 150 days, the lender must attempt to contact the borrower by telephone every 30 days. If unsuccessful, at least one more forceful collection letter must be sent during each 30-day period.
- When a loan is delinquent by 151 to 180 days, the lender must send a final demand letter (if the borrower's address is known) requiring payment in full within 30 days and notifying the borrower that a default will be reported to national credit bureaus.
- The lender must use normal commercial skip-tracing techniques which include contacting any references and cosigners to locate a borrower whose address is unknown.
- Before filing a default claim, the lender must request assistance from the guarantee agency (preclaims assistance), if available.

In addition to conducting due-diligence procedures lenders should take the following steps:

- Work with the educational institutions to obtain information on the student's whereabouts. After graduating, student borrowers are very mobile, and extra effort must be made to locate them.
- Use any supplemental preclaims assistance offered by the guarantee agency.
- Contact delinquent borrowers more often than is required.

- Telephone borrowers on weekends and evenings if they cannot be reached during the day.
- Consider rescheduling a student's loan so that repayment coincides with a time when the borrower will most likely be able to repay (e.g., right after the borrower receives a paycheck).
- Offer graduated repayment schedules to borrowers.
- Be flexible—if a borrower is willing but unable to make the monthly payment, consider offering the borrower forbearance.

Recommendation #4
Carefully monitor loan servicers.

Lenders who use loan servicing contractors to help them in collections must ensure that the servicers follow the same due-diligence procedures that lenders are required to follow—sending timely collection notices, using skip-tracing techniques to locate borrowers, and requesting preclaims assistance from the guarantee agency.

If these procedures are not followed properly, the federal government will withdraw its guarantee for the loans. Thus lenders are ultimately held financially responsible for servicers who do not adequately collect their loans.

To ensure that their loans will be federally guaranteed, lenders should periodically audit and review their servicers' operations to make sure that federal regulations regarding delinquent borrowers are being followed. If they are not, the lenders must step in and begin servicing these loans themselves or hire another servicer.

PART IV

WHAT GUARANTEE AGENCIES CAN DO

Default and the Guarantee Agency

Guarantee agencies conduct a variety of activities that include reviewing schools and lenders, establishing and enforcing program requirements, such as due-diligence, providing preclaims and supplemental preclaims assistance, reviewing and paying default claims filed by lenders, collecting defaulted loans, and disseminating program material and information.

If due-diligence requirements are met, guarantee agencies will reimburse lenders for their default claims. In turn, the Department of Education reimburses a guarantee agency for a percentage of these claims, ranging from 80 to 100 percent. At the beginning of each fiscal year, every agency receives 100 percent reinsurance of default claims. However, when reinsurance claims paid to the agency during any fiscal year reach five percent of the agency's total amount of loans in repayment at the end of the preceding fiscal year, the agency's reinsurance rate drops to 90 percent. When claims reach nine percent, the agency's reinsurance rate drops to 80 percent. In fiscal year 1988, twelve guarantee agencies hit the 90 percent trigger and, of those twelve, three hit later the 80 percent rate.

Clearly, guarantee agencies have a financial incentive to reduce defaults. Many agencies have, in fact, implemented comprehensive default reduction initiatives. Some, however, have not. The pages ahead outline actions guarantee agencies can take to prevent defaults from occurring.

Guarantee agencies not only have a financial incentive to reduce defaults but also to recover loans that have already entered default. A guarantee agency is permitted to retain 30 percent of its collections on a loan, plus 10 percent for a loan reinsured at 90 percent, or 20 percent for an 80 percent reinsured loan. Guarantee agencies collected $539 million in FY 1988.

A 1986 study[1] that analyzed guarantee collections found that agencies were able to collect on 27 percent of defaulted cases within six months of paying the claim and 34 percent of cases that had been in collection 18 months.

The study determined the following:

- Early collection efforts are most successful when letters and follow-up telephone calls are used.
- Tax refund offsets are an effective method of obtaining direct payments and also of inducing borrowers to make voluntary payments.
- Wage garnishment is very successful in obtaining payments from those borrowers who could legally be subjected to it.

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1 Applied Management Sciences, Inc., *A Demonstration of Behavior Scoring Models to Prevent Defaults and to Collect Defaulted Loans in the Guaranteed Student Loan Program*, 1986.

- Legal action is an effective technique for obtaining payments as a last resort.

In summary, persistence is strongly related to recovery success and collections can be successful on resistant borrowers, even years after default.

Recommendation #1
Monitor lenders and postsecondary institutions and fully enforce all established laws and regulations.

Many guarantee agencies are taking strong action to reduce defaults in their regions. By monitoring lenders and educational institutions, to ensure that they are properly administering the student loan program and adequately preventing defaults, they are serving notice that high defaults will not be permitted in their jurisdiction. Some guarantee agencies are penalizing and even bringing legal proceedings against lenders and institutions that are not complying with the law, to ensure that only legitimate ones participate in the program and to deter future violations.

Guarantee agencies must take the following steps:

- Ensure that lenders are following due-diligence procedures. All lenders participating in the program are required by regulation to follow these practices.
- Target audits at high-default schools. A high default rate signals a problem at the school that should be investigated.
- Conduct thorough on-site reviews.
- Establish stringent administrative compliance criteria and sanctions for noncompliance.
- Enforce sanctions against lenders who violate the guarantee agency's established terms and conditions under which claims are paid.

MONITORING LENDERS AND INSTITUTIONS: New Jersey Higher Education Assistance Authority

In 1986, the New Jersey Higher Education Assistance Authority (NJHEAA) developed a plan for systematically auditing institutions. At that time, NJHEAA was concerned that institutions with serious administrative deficiencies were eligible to participate in the GSL programs.

Under their compliance plan, NJHEAA identifies schools with high default rates and notifies them of their intent to conduct a program review at their institution. These institutions are evaluated on how they perform in the following six categories:

1. Student withdrawal rate
2. Non-notification of required enrollment status changes to GSL lenders and NJHEAA
3. Incomplete documentation
4. Files missing entirely
5. Late refunds
6. Refunds never paid

Using the percentage in each category, NJHEAA calculates a "Noncompliance Index" for the institution to determine the sanction. These percentages constitute "violation points" that are weighted by multiplying the percentage of missing files and refunds never paid by four, and the percentage of incomplete files and late refunds by two. The index is equal to the sum of the weighted violation points divided by the number of categories. The following sanctions are imposed based on this index:

Noncompliance Index	Sanction
9.9 or less	None
10.0 to 14.9	Plan of Corrective Action
15.0 to 24.9	Limitation for 9 months
25.0 to 34.9	Limitation for 18 months
35.0 to 69.9	Suspension for 18 months
70.0 and above	Termination

By developing a precise measure for noncompliance and defined sanctions, NJHEAA can systematically evaluate institutions. Since 1985, 40 New Jersey institutions participating in the program have closed, including half of those that were audited.

Recommendation #2
Help institutions in their default reduction efforts.

As noted earlier, institutions are required to conduct entrance and exit interviews to participate in the student loan programs. Also, high-default institutions are required to take other specified actions to reduce their default rates. Guarantee agencies can assist institutions in their endeavors by taking the following actions:

- Produce and distribute debt management materials, such as pamphlets, videotapes, and posters, that institutions can use in their entrance and exit interviews.
- Provide training and technical assistance to financial aid administrators.
- Keep institutions abreast of regulatory changes that affect them.
- Notify institutions of delinquent borrowers during the preclaims period before the borrowers enter default. Institutions may be able to encourage borrowers to repay their loans and contact lenders with more up-to-date address information.

HELPING INSTITUTIONS REDUCE DEFAULTS: Massachusetts Higher Education Assistance Corporation

In 1983, the Massachusetts Higher Education Assistance Corporation (MHEAC) formed a loan-counseling task force to review literature, studies, and current models; identify experts in the field; and create a comprehensive loan-counseling model, if necessary, to encourage secondary and postsecondary institutions to provide financial debt management materials to meet the needs of their students. The task force is composed of representatives from the lending community, postsecondary institutions, high school guidance offices, loan servicing organizations, and MHEAC staff.

The task force's first order of business was to develop an agreed-on set of principles. After reviewing the existing research and literature on student loans and student loan counseling, the task force reached the following conclusions:

- *Ability* to repay is not the only important attribute for repaying loans; *willingness* to repay is also very important.
- Loan counseling must include a discussion of how debt relates to future earnings and lifestyle choices.
- Loan counseling must encourage students to consider alternatives to borrowing.
- The first payment is the most important. Most defaults are attributabl to borrowers who never make the first payment.

With these basic principles established, the task force began to develop materials methods, and procedures for improving loan-counseling skills and techniques. The group commissioned reports on consumption patterns, developed materials (including posters, brochures, and videos) on loan borrowing, implemented a repayment hotline to assist potential defaulters, and established a speakers bureau for counseling high school seniors and their parents on financial aid. One of their more successful publications, a comprehensive booklet titled *Educational Loans: It's your Choice*, along with supplemental brochures and handouts that accompany this booklet, explain to students in a clear and well-organized way everything from budgeting expenses to alternatives to default.

Recommendation #3
Help lenders collect repayments before loans enter default.

On some loans, a lender must turn to the guarantee agencies for authority and borrower information that is not at the lender's disposal. To help lenders, guarantee agencies can take the following steps:

- Provide training and technical assistance to lenders.
- Investigate effective collection techniques.
- Provide lenders with information on the postsecondary institutions, such as default rates, job placement rates, and dropout rates, to assist them in evaluating the institutions before loan funds are distributed.
- Help support effective tracking of student status.
- Provide effective preclaims and supplemental preclaims assistance.
- If state law permits, get information on borrowers' whereabouts from the state's department of motor vehicles, tax department, employee register, and unemployment commission.
- Publicize the consequences of default.

Recommendation #4
If loans enter default, pursue collections diligently.

After loans enter default, the responsibility for collections lies with the guarantee agencies. Although effective collection procedures may differ by region (e.g., California has found that using bilingual collectors in predominantly Hispanic areas improves collection), the following recommendations apply to all guarantee agencies:

- Train all collectors in the Guaranteed Student Loan programs. Collectors should know the rules and regulations of the student loan programs if they are to collect repayments effectively.
- Contact defaulters frequently through letters, phone calls, or private collection agents.
- Consider automating the collections procedure. Guarantee agencies can save time and money by automatically scheduling accounts to be worked and by using auto-dialers to eliminate wasted time on no answers and busy signals.
- Pursue cosigners equally. The cosigners (usually parents) are often in a better position to repay loans.
- Seek authority for and implement programs of state tax-refund offsets and wage garnishment.
- Pursue litigation when appropriate.
- Participate fully in the federal income tax-refund offset program by referring all available accounts that are not in repayment status to the Department of Education for potential offset by the Internal Revenue Service.

PURSUING COLLECTIONS DILIGENTLY: ***Pennsylvania Higher Education Assistance Agency***

In 1982, the Pennsylvania state legislature passed a law enabling the Pennsylvan Higher Education Assistance Agency (PHEAA) to garnish wages without going through ordinary court procedures while still maintaining the concept of due process. PHEAA takes the following steps when borrowers become delinquent:

- *The possibility of wage garnishment is used to deter possible defaulters.* When loan recipients are delinquent by two to four months, they are informed that PHEAA may bring a lawsuit against them to force repayment of the loan. Borrowers who are delinquent by four to eight months are contacted several additional times and warned that "legal action including the attachment of [their] wages" can result if they do not voluntarily repay their loans.
- *Loans that are in default enter the next stage.* PHEAA conducts a computer check of the defaulter's employment status with the state's employment records. If the borrower is employed and is earning a salary above the poverty level, wage garnishment procedures are initiated. This automated system is able to process a great number of cases for a cost that amounts to no more than ordinary billing costs.
- *The loan defaulter is informed of the proceedings* and has 30 days to dispute the debt. In an average year, only about 30 out of every 10,000 cases are disputed. In the case of a dispute, there is no need to wait for an open court date; an independent hearing is held at PHEAA with a local lawyer serving as an independent hearing examiner on the case.
- *If no dispute occurs, or if a dispute is resolved in favor of PHEAA, the employer is presented with the claim and is required by law to garnish the loan defaulter's wages.* Depending on the amount of the debt and the defaulter's wages, up to 10 percent of the defaulter's income is withheld.

Before the legislation was enacted, 50 cases of wage garnishment a week were processed through the ordinary court procedures. Since enactment of this policy, approximately 400 defaulters a week have had their wages garnished. In the six years before 1983 when these streamlined wage garnishment procedures were in plemented, a total of only about $1.8 million in wages was collected, an average of $300,000 each year. In 1984, the first year after the new procedures went into effect, almost $1.5 million was collected. The dollar amounts collected have con tinued to rise each year, so that between January and June of 1989, more than $6.8 million was collected. Furthermore, the state's costs associated with gar nishing wages have plummeted.

PART V

WHAT ACCREDITING AGENCIES CAN DO

Recommendation #1
Assess educational quality when reviewing postsecondary institutions for accreditation.

Without accreditation by a nationally recognized agency, educational institutions are generally not eligible for any student aid or other federal education funds. Thus stringent assessment by accrediting agencies can ensure that student loan funds are distributed only to institutions that offer students a good education. Accrediting agencies should develop a systematic method for dete mining whether students are learning at institutions before continuing to accredit these institutions. Such a method should include the following steps:

- Require institutions to document student achievement as a condition for accreditation. Measurements of student achievement include retention, job placement, admissions into graduate or professional schools, and success on licensure or certification examinations.
- Ensure that institutions are truthful about costs, refund policies, graduation requirements, and any claims made in catalogues, advertisements, and other materials given to prospective students. Institutions that make such claims should be able to back this information with documentation.
- Ensure that institutions counsel or test students who seek to begin their studies without having a high school degree or GED.
- Stringently evaluate the institution's facilities, teachers' qualifications, curriculum, and program of studies.
- Periodically reexamine the accreditation standards and procedures to ensure that they serve the student, and not the institution seeking accreditation.

Recommendation #2
Evaluate the administrative capability of institutions.

Accreditation not only serves as a symbol of quality assurance for parents and students but implies that an institution has achieved a certain level of program effectiveness, financial integrity, and administrative efficiency. Accreditation often ignores the administrative structure of an institution, though this is important for an institution's overall performance. Accrediting agencies should take the following actions:

- Visit institutions to ensure that the schools comply with standards for institutional eligibility.
- Validate the course length of its institutions. Title IV financial aid is tied to course length, resulting in a number of institutions "stretching" their curricula for the purpose of qualifying for Title IV aid.
- Do not automatically accredit branch campuses. All institutions should be thoroughly reviewed before being accredited.
- If schools are not complying with established standards, promptly revoke the institution's accreditation.
- Refuse accreditation for two years to any school that loses its accreditation.

PART VI

WHAT STATES CAN DO

Recommendation #1
Establish and enforce stringent licensing and approval procedures for postsecondary institutions.

States may set educational, fiscal, and administrative requirements that all in stitutions in that state must meet. Studies on state oversight indicate that mai states are not evaluating institutions as effectively as they could be.

According to one report,[1] a review of state oversight activities revealed "the patchwork effect... the lack of clear definitions, and the confusing array of state agencies involved." For example, many states have numerous agencies volved in oversight ranging from the Department of Motor Vehicles, which licenses and regulates truck driving schools, to the Board of Cosmetology, which oversees cosmetology schools. Often, these agencies serve primarily i a different capacity and do not have the expertise to regulate and license institutions.

States must develop strict requirements for licensing and regulating institutions to help curb fraud and abuse by some institutions. States should take th following steps:

- Coordinate activities with all state agencies that license and regulate institutions in the state.
- Implement tighter business-licensing requirements for all educational institutions to eliminate institutions that cannot provide the education promised by the institution and do not maintain adequate fiscal and administrative controls.
- Ensure that institutions are financially sound. Many state agencies require institutions to post bonds to protect students if programs are discontinued or institutions closed. States may also require institutions to have teachout arrangements with other institutions. Some states have or are considering tuition recovery plans, whereby institutions are required to pay into an insurance fund that is used to refund tuition to students when institutions close.
- Keep statistics that measure institutions' quality; these should include program completion, job placement, and licensing pass rates.

1 State Higher Education Executive Officers, *State Oversight of the Private and Proprietary Sector*, 1985.

- Require fair tuition refund policies. A pro-rata refund policy or similar type of policy can be quite effective at reducing default costs associated with dropouts.
- Designate a unit of state government to detect, investigate, and prosecute student financial aid crimes and frauds.

ENFORCING STRINGENT LICENSING OF INSTITUTIONS: New York State Education Department's Bureau of Proprietary School Supervision

The New York State Education Department's Bureau of Proprietary School Supervision is responsible for regulating all aspects of private trade and business schools in New York State. The Bureau completes its mission by addressing the following three areas:

1. *Education*—The Bureau is responsible for ensuring that educational programs of the proprietary schools meet minimum standards through curriculum approval and on-site monitoring of the schools's programs
2. *Licensing*—The Bureau licenses all schools, teachers, school directors and school agents (recruiters). The Bureau also approves all school advertising prior to its use.
3. *Investigations*—The Bureau conducts investigations and audits of proprietary schools to ensure compliance with education laws and the Commissioner's regulations.

The overall goal of the Bureau is to ensure that the educational programs in proprietary schools meet the needs and expectations of their students. To meet it goal the Bureau—

—establishes entrance requirements which applicants to proprietary schools must pass in order to become eligible for enrollment;

—reviews and approves all curricula in proprietary schools;

—ensures that all teachers and directors meet the necessary educational qualifications in order to be licensed in the State of New York;

—pre-approves all advertising to be used by proprietary schools to ensure that all information presented to students is a fair and accurate representation of the school's programs;

—conducts on-site monitoring of the educational quality of the proprietary school programs;

—pre-approves the school's catalog, enrollment agreements, financial statements, attendance and record procedures, and facilities;

—investigates all complaints made against proprietary schools;

—conducts in-depth investigations of all schools found in violation of education laws or the Commissioner's regulations; and

—takes disciplinary action against all schools in violation of education laws or the Commissioner's regulations. Such action can include written reprimands, fines, suspension, and/or revocation of a school's license.

Recommendation #2
Take strong action against defaulters.

Governors and state legislators must send a strong message to students, postsecondary institutions, and lenders that high defaults will not be tolerated. To do this they must ensure that guarantee agencies have the support and the legislation necessary to pursue defaulters aggressively. For example, many states have enacted legislation to give guarantee agencies more authority to collect on delinquent and defaulted loans. States can also enact legislation to deny professional licenses and state jobs to defaulters until they make adequate repayment arrangements.

States should take the following steps:

- Enact a state tax-refund offset program. The federal government has collected approximately $637.3 million from 1.16 million people since 1986 to offset defaulters' federal tax refunds. States can enact similar programs by offsetting defaulters' state tax refunds.
- Enact a wage garnishment program. A well-designed wage garnishment program can increase collections at very little cost while still maintaining due process.
- Deny professional licenses to defaulters until they take steps to repayment.
- Screen potential applicants for state jobs to prevent the hiring of loan defaulters who have not entered into repayment agreements.
- Ensure that information available at other state agencies, such as the Department of Motor Vehicles, the tax department, and the unemployment commission, is available to the guarantee agency.

PART VII

FEDERAL GOVERNMENT RESPONSIBILITIES

The federal government must guide and assist schools, lenders, and guarantee agencies in reducing student loan defaults and must protect the integrity of the Guaranteed Student Loan programs by ensuring that all appropriated funds are used to further students' education. Clearly, defaults are a misuse of these funds.

To stop abuses in the student loan program and to reduce defaults, the Department of Education has moved on several fronts. The Department has taken and will continue to take every action allowed by law—administrative, regulatory and legislative—to discourage defaults and improve collections. These include the following actions to intensify default prevention and collection efforts:

- *Training.* The Department is improving the training of persons who administer the Guaranteed Student Loan programs.
- *Research.* The Department will continue to conduct studies on default behavior and effective collection techniques. As research results become available the Department will disseminate results.
- *Dissemination of information.* The Department will also disseminate information on job placement, program completion, and certification pass rates for nonbaccalaureate vocational schools and state and professional licensure requirements.
- *Toll-free hotline.* The Department will publicize 1-800-MIS-USED, its toll-free fraud and abuse hotline for students and the public, more extensively in future publications.
- *Audits and investigations.* The Department's Office of the Inspector General (OIG) investigates institutions that have very high default rates, those that have been the subject of complaints, and any others that the Department has reason to believe may be guilty of fraud or abuse. OIG will be conducting more audits and investigations of schools suspected of fraudulent or unfair practices.
- *Due-diligence regulations.* The Department requires lenders and guarantee agencies to make specific efforts to follow-up on delinquent loans before they enter default status.
- *Credit bureau reporting.* The Department reports Department-held defaults to consumer credit bureaus in order to prevent defaulters from obtaining credit financing until they have made satisfactory arrangements for repayment.
- *IRS offsets.* The Department refers defaulted accounts to the IRS which withholds the tax refunds of defaulters to pay for their student loan debt.

- *Skip tracing.* The Department has rigorously pursued borrowers by matching the location of borrowers who have moved with the IRS address files.
- *Federal employee salary offset.* The Department refers defaulted accounts belonging to federal employees to their employing agencies for salary offset.
- *Justice Department referrals.* The Department of Education refers defaulted accounts to the Justice Department for litigation. In addition, the Justice Department is implementing the recently enacted authority to contract with private attorneys to litigate against defaulters.
- *Collection services.* The Department has expanded the number of contracts with private-sector collection agencies to collect on defaulted student loans.
- *Collection costs.* The Department charges borrowers for collection costs it incurs in enforcing defaulted student loans that it holds.
- *Regulatory actions.* The Department of Education published a final regulation on GSL defaults, which required institutions to take specific default-reduction actions dependent upon their default rates. The Department will continue to regulate where necessary to reduce defaults.
- *Default-related legislation.* The Executive Branch of the federal government has proposed, and will continue to propose, default reduction and collection improvement measures.

PART VIII

APPENDICES

Appendix A:
Borrowers' Rights and Responsibilities

Borrowers' Rights

Each borrower who takes out a loan, signs a promissory note, in which tl rower agrees to repay the loan. The promissory note is a legally binding ment. The borrower must receive a copy of this note upon signing it; the original note must be returned to the borrower when the loan is paid in fu

Each borrower has the right to a grace period before repayment period bc if the loan provides for one. The grace period starts when the borrower le school or drops below half-time status. The exact length of the grace peri shown on the promissory note.

If a borrower has a Stafford Loan or an SLS, the loan proceeds must be n payable to the borrower or to both the borrower and the postsecondary in tion.

Before the postsecondary institution gives a borrower the first loan disbu ment, the lender must give the borrower the following information about loan:

- The full amount of the loan, the interest rate, and when the borrower must start repaying.
- The effect that borrowing will have on eligibility for other types financial aid.
- A complete list of any charges to the borrower (loan fees) and inf mation on how those charges are collected.
- The yearly and total amounts the student can borrow and the max mum and minimum repayment periods.
- A current description of loans the borrower owes to the postsecon dary institution or the lender and estimates of the total debt and monthly payments.
- An explanation of default and its consequences. One of those con sequences will be that the default will be reported to a credit bureau. Such a report may harm the borrower's credit rating.
- An explanation of refinancing and consolidation options and of th option to prepay the loan at any time without penalty.

Before the borrower's repayment period begins, the postsecondary institution/lender must tell the borrower—

—the amount of total debt (principal and interest), the interest rate, ar the total interest charges on the loan;

—the name of the borrower's lender, where to send the payments, and whom to write if the borrower has questions about the loan;

—what fees the borrower should expect during the repayment period; and

—prepayment, refinancing, and consolidation options.

The borrower also must receive a loan repayment schedule detailing the date when the first payment is due and the number, frequency, and amount of all payments.

Borrowers who have Stafford Loans, have a right to federal interest benefits, if qualified. That is, the federal government will pay the interest on the loan until the repayment period begins and during authorized deferment periods. (A borrower who does not qualify for federal interest benefits must arrange with the lender to pay the interest of the Stafford Loan.)

A lender who sells the loan or transfers the right to receive payments must so notify the borrower.

Borrowers' Responsibilities

The borrower is the individual primarily responsible for the loan's repayment.

The borrower must keep the school informed of all address changes while in school.

The borrower must notify the lender if the borrower—

—does not enroll in school for the period for which the loan was intended;

—graduates, withdraws from school, or drops below half-time status;

—transfers to another institution; or

—changes his or her name, address, or Social Security number.

The borrower must repay the loan according to the repayment schedule.

The borrower must make payments on the loan even if the borrower does not receive a bill. Billing statements (or coupon books) are sent as a convenience to the borrower, but not receiving such statements does not relieve the borrower of the obligation to make payments.

The borrower should always include the Social Security number on all correspondence to the lender (including payment checks).

The borrower should notify the lender of any circumstance that affects the borrower's ability to repay the loan or eligibility for deferment or cancellation.

The borrower should remember that the loan money can be used only for tuition and other related educational expenses.

Before leaving school, each borrower should attend an exit interview.

Appendix B:
Ramifications of Default

Student loan defaults not only cost the federal government billions of dollars, they hurt the borrower. Guarantee agencies, the state, and the federal government all may take action against defaulters. Defaulters can even be sued.

Borrowers should expect the following to occur if they default:

- Report of the default to national credit bureaus, meaning a damaged credit rating for at least seven years.
- The loss of generous repayment and deferment options.
- Possible withholding of federal and state income tax refunds to satisfy the loan obligation.
- Exposure to civil suit.
- Liability for collection costs, court costs, and attorney fees.
- Possible referral of the account to a collection agency.
- Garnishment of wages if the borrower's guarantee agency garnishes wages or if the borrower is a federal employee.
- Loss of eligibility for further federal Title IV student assistance.
- Loss of eligibility for other types of government loans, such as Small Business Administration or Veterans Administration loans or federally subsidized mortgages.

In the end, defaulters can be required to repay substantially more than the amount they would have had to pay if they had not defaulted.

Appendix C:
Sample Repayment Table

MONTHLY PAYMENTS[1]
(based on 10-year repayment schedule and $50 minimum payment)

Total Balance	*8%*	*9%*	*10%*	*12%*	*14%*
$1,000	$50.00	$50.00	$50.00	$50.00	$50.00
2,000	50.00	50.00	50.00	50.00	50.00
3,000	50.00	50.00	50.00	50.00	50.00
4,000	50.00	50.68	52.87	57.39	62.11
5,000	60.67	63.34	66.08	71.74	77.64
6,000	72.80	76.01	79.30	86.09	93.16
7,000	84.93	88.68	92.51	100.43	108.69
8,000	97.07	101.35	105.73	114.78	124.22
9,000	109.20	114.01	118.94	129.13	139.74
10,000	121.33	126.68	132.16	143.48	155.27
15,000	182.00	190.02	198.23	215.21	232.90
20,000	242.66	253.36	264.31	286.95	310.54
25,000	303.32	316.69	330.38	358.68	388.17
30,000	363.99	380.03	396.46	430.42	465.80
35,000	424.65	443.37	462.53	502.15	543.44
40,000	485.32	506.71	528.61	573.89	621.07
45,000	545.98	570.05	594.68	645.62	698.70
50,000	606.64	633.38	660.76	717.36	776.34

1 This represents the lowest possible monthly payment. Not all lenders give 10 years to repay.

Appendix D: Sample Budget Worksheets

IN-SCHOOL BUDGET WORKSHEET

Yearly Resources	
Family contribution	______
Financial assistance	______
Savings	______
Yearly earnings	______
Non-taxable income	______
Other	______
Total Resources	______

Yearly Expenses	
Education expenses:	
Tuition	______
Books, fees, and supplies	______
Housing expenses:	
Rent	______
Utilities	______
Food	______
Transportation:	
Gas/oil	______
Car payments	______
Car insurance	______
Car repairs	______
Bus/train/air	______
Health:	
Insurance	______
Doctor	______
Dentist	______
Prescription drugs	______
Clothing	______
Miscellaneous:	
Entertainment	______
Personal items	______
Child care	______
Savings	______
Other	______
Total Expenses	______

OUT-OF SCHOOL BUDGET WORKSHEET

Yearly Resources	
Expected Salary	______
Less taxes	______
Savings	______
Total Resources	______

Yearly Expenses	
Housing expenses:	
Rent	______
Mortgage Payment	______
Utilities	______
Furnishings	______
Food	______
Transportation:	
Gas/oil	______
Car payments	______
Car insurance	______
Car repairs	______
Bus/train/air	______
Health:	
Insurance	______
Doctor	______
Dentist	______
Prescription drugs	
Miscellaneous:	
Entertainment	______
Personal items	______
Child care	______
Savings	______
Student loan payments	______
Other	______
Total Expenses	______

Appendix D: Sample Budget Worksheets

IN-SCHOOL BUDGET WORKSHEET

Yearly Resources	
Family contribution	______
Financial assistance	______
Savings	______
Yearly earnings	______
Non-taxable income	______
Other	______
Total Resources	______

Yearly Expenses	
Education expenses:	
Tuition	______
Books, fees, and supplies	______
Housing expenses:	
Rent	______
Utilities	______
Food	______
Transportation:	
Gas/oil	______
Car payments	______
Car insurance	______
Car repairs	______
Bus/train/air	______
Health:	
Insurance	______
Doctor	______
Dentist	______
Prescription drugs	______
Clothing	______
Miscellaneous:	
Entertainment	______
Personal items	______
Child care	______
Savings	______
Other	______
Total Expenses	______

OUT-OF SCHOOL BUDGET WORKSHEET

Yearly Resources		***Yearly Expenses***	
Expected Salary	______	*Housing expenses:*	
Less taxes	______	Rent	______
Savings	______	Mortgage Payment	______
Total Resources	______	Utilities	______
		Furnishings	______
		Food	______
		Transportation:	
		Gas/oil	______
		Car payments	______
		Car insurance	______
		Car repairs	______
		Bus/train/air	______
		Health:	
		Insurance	______
		Doctor	______
		Dentist	______
		Prescription drugs	
		Miscellaneous:	
		Entertainment	______
		Personal items	______
		Child care	______
		Savings	______
		Student loan payments	______
		Other	______
		Total Expenses	______

Appendix E:
Options for Repayment

Institutions and lenders should inform borrowers who are having problems with repayment about the options that are available. A borrower who qualifies may be able to defer payment; have a portion or all of the loan canceled; have a portion or all of the loan repaid on the borrower's behalf by a third party; or enter forbearance with the lender, if the lender deems forbearance appropriate.

Deferment

Deferment periods are periods during which the payment of principal is postponed and the interest is paid by the federal government. A borrower who meets the specific requirements has a legal right to postpone student loan repayment for a particular period of time.

A borrower may defer repayment under any of the following circumstances:

- Attending a GSL eligible institution on a full-time basis or, for new borrowers (borrowers who had no outstanding loans on the date they signed the promissory note for a loan that was either disbursed on or after July 1, 1987 or was for a period of enrollment that began on or after July 1, 1987), on a half-time basis.
- Studying in an eligible graduate fellowship program or in a rehabilitation training program for disabled persons.
- Participating in an internship program that either is required to begin professional practice or leads to a degree or certificate (two-year limit).
- A member of the armed forces (three-year limit).
- A volunteer in the Peace Corps, ACTION, or comparable tax-exempt organization (three-year limit).
- Engaged as a full-time teacher in a public or nonprofit private elementary or secondary school in an area designated by the Department of Education as having a teacher shortage (three-year limit).
- Serving as an active-duty member of the National Oceanic and Atmospheric Administration Corps or as an officer in the Commissioned Corps of the Public Health Service (three-year limit).
- Conscientiously seeking but unable to find employment (two-year limit).
- Temporarily totally disabled or caring for a temporarily totally disabled dependent or spouse (three-year limit).
- On parental leave (six-month limit).

- A mother of a preschool age child who earns no more than $1 over the minimum wage (one-year limit).

Forbearance

Forbearance is the temporary suspension of full or partial payments. A borrower who is willing but financially unable to make the loan repayment may request forbearance from the lender, which the lender may or may not grant. The lender may grant forbearance of principal, interest, or both, for a particular period of time. Unlike the case of deferment, interest continues to accrue during this period.

Cancellation

The Department of Education cancels Guaranteed Student Loans only if the borrower dies or becomes permanently and totally disabled.

The Department will also pay in full or in part a loan discharged in bankruptcy.

Repayment by a Third Party

Sometimes an outside party will make payments on behalf of a student borrower, often for service rendered by the borrower. The following organizations may repay student loans:

- The Department of Defense, for borrowers who are members of the Army or National Guard.
- Several states repay student loans for borrowers who work in "shortage professions," such as math and science teaching and the health professions, and for borrowers who work in manpower shortage areas.

Appendix F: Glossary

Ability to benefit: The criteria under which students lacking a high school degree or general educational development (GED) certificate are admitted to postsecondary institutions and allowed to receive aid (other than Supplemental Loans for Students). Ability-to-benefit students must (1) pass a standardized admissions test, (2) enroll in and successfully complete a remedial program if the student fails the admissions test or if the student is admitted on the basis of counseling, or (3) receive a GED by the end of the first year of the course of study or before graduation or certification, whichever is earlier.

Accrued interest: Interest that accumulates, is payable at a later date, and may be capitalized.

Cancellation: A repayment by the Secretary of the balance of a borrower's loan, due to total and permanent disability or death.

Certification: The process through which the institution confirms in writing the student's eligibility for a loan.

Clock-hour schools: A school, generally a proprietary institution, that offers short-term programs and measures academic progress or attendance in terms of the clock-hours spent in training.

Collection agency: A firm or organization that specializes in debt collection.

Consolidation loan: A loan made for the purpose of paying off loans received while a borrower was attending school. The consolidation loan usually has a lower monthly payment, a higher interest rate, and a longer repayment period than the loans which it pays off.

Cosigner: A person who signs a loan note with the borrower and thereby agrees to repay the loan if the borrower defaults.

Cumulative default rate: One of several measures of the propensity to default; this measure is calculated by dividing the dollar value of all loans that have ever defaulted since the program began by the dollar value of all loans that have ever entered repayment status. ...entage can also be calculated using borrowers rather

Default: Failure to repay a student loan according to the terms agreed to in the promissory note. In the GSL programs, default generally occurs when a loan payable in monthly installments is 180 days delinquent.

Deferment: Suspension of required loan payments for specified periods during which the borrower is engaged in further schooling, military service, or other specified activities.

Delinquent status: The status of a loan when a payment is not made by the due date.

Disbursement: The distribution of loan proceeds to the borrower.

Due-diligence procedures: Servicing requirements in federal regulations with which lenders must comply to maintain the federal guarantee on a student loan.

Fiscal year cohort default rate: One of several measures of the propensity to default; this measure is the percentage of borrowers entering repayment status in one fiscal year who default before the end of the following fiscal year. This percentage can also be calculated using dollars.

Forbearance: Temporary suspension or reduction of principal and/or interest payment, granted at the lender's discretion. The borrower must demonstrate to the lender his or her willingness but inability to make payment during a period of hardship.

General educational development (GED) certificate: Certificates awarded to students who pass the GED examination in lieu of receiving a high school diploma. This examination is designed to appraise students' achievement or performance in the broad subject-matter areas usually required for high school graduation.

Grace period: Period between the date borrowers cease at least half-time attendance and the date they enter repayment status, usually six to nine months.

Graduated repayment schedule: Payment schedule that offers low payments in the initial years of repayment and increased payments in subsequent years.

Guarantee agency: An organization that administers the Stafford Loan, PLUS, and Supplemental Loans for Students (SLS) programs.

One of the purposes of a guarantee agency is to insure lenders against losses due to borrower defaults.

Guaranteed Student Loan (GSL) programs: Group of programs comprised of the Stafford loan, the PLUS, and the Supplemental Loans for Students (SLS) programs. (See specific loan program definitions).

In-school period: Period between the date the student begins school and the date the student leaves grace status.

Insurance Fee: Fee the guarantee agency may charge lenders to help cover the agency's expenses. Lenders may pass the charge on to their borrowers.

Interest capitalization: Procedure whereby loan repayment is deferred but interest continues to accrue and is combined with the original loan principal, thus increasing the borrower's debt.

Limitation, suspension and termination (LS&T): A procedure whereby a school or lender that fails appropriately to administer the GSL programs may be subject to penalties, including limitation on the amount of loans, suspension of the institution from participation in the GSL programs for a specified time period, or termination of the institution's participation.

Loan principal: Total amount borrowed, not including interest.

Origination fee: An amount generally equal to 5 percent on the face value of the loan which is deducted from each loan made to the student and transferred to the Department to help offset loan subsidy costs.

PLUS loans: Variable-rate, generally unsubsidized loans for parents to help pay for their children's education.

Preclaims assistance: Assistance provided to lenders by the guarantee agency to encourage delinquent borrowers to make payments anc to help locate borrowers after an account is delinquent.

Promissory note: The written agreement a borrower signs to record the promise to repay the loan. The note lists the terms on which the borrower agrees to pay back the loan.

Proprietary school: A for-profit school, usually offering trade or technical programs two years or less in length.

Pro-rata refund policy: A refund policy for a student who withdraws, under which a school refunds a percentage of the tuition, fees, room and board, and other school charges less any unpaid charges and less a reasonable administrative fee. This percentage is equal to the period remaining in the term divided by the total enrollment period.

Reinsurance payments: The payment made by the federal government to guarantee agencies for defaulted claims.

Repayment schedule: The form provided by the lender to students, detailing the monthly payment, the dates when payments are due, and the total amount owed.

Repayment status: The status of a loan or borrower that occurs once the borrower has left school and completed the grace period and during which repayments are generally due on the loan.

Secondary market: Organizations that buy student loans from the original lender or from other loan holders.

Servicer: An organization, often hired by lenders, that handles loan billing and other activities on current and delinquent, but not defaulted, loans.

Skip tracing: Procedure used to locate borrowers when addresses are unknown that often involves computer matches with other consumer files.

Stafford loans: Subsidized, need-based loans to undergraduate and graduate students for postsecondary study.

Supplemental Loans for Students (SLS): Variable-rate, generally unsubsidized, loans for graduate, independent undergraduate, and, in certain instances, dependent undergraduate students.

Supplemental preclaims assistance: Assistance provided to lenders by the guarantee agency to encourage delinquent borrowers to repay and to help locate borrowers in connection with a loan on which the guarantor has exercised preclaims assistance and which has been in delinquent status for at least 120 days.

Wage garnishment: The procedure used to deduct loan payments from defaulters' wages.

Acknowledgments

This handbook was written by Mary Farrell, of the U.S. Department of Education, with contributions from the following U.S. Department of Education employees:

Alan Ginsburg
Tyndall Greene
Maureen McLaughlin
Nina Winkler

The Department of Education wishes to thank Pelavin Associates for their assistance in developing this handbook.

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